S&P Global

Research Update:

Wendel SE Outlook Revised To Negative On Increasing LTV From The Planned Acquisition Of Monroe Capital; Ratings Affirmed

October 31, 2024

Rating Action Overview

- Wendel SE entered a definitive agreement to acquire 75% of U.S.-based private debt asset manager Monroe Capital for an initial consideration of $1.13 billion and a closing expected in the first half of 2025.
- Pro forma this transaction, we estimate that Wendel's S&P Global Ratings-adjusted loan-to-value (LTV) ratio is increasing to 21%-23%, above our 20% rating downside trigger.
- At the same time, we anticipate that the investment holding will target to deleverage organically in the next 12-18 months to restore financial flexibility.
- We therefore revised our outlook on Wendel to negative from stable and affirmed our 'BBB' long-term issuer and issue credit ratings on its unsecured debt as well as its 'A-2' short-term rating.
- The negative outlook indicates that we could lower our rating on Wendel if it fails to restore adequate LTV headroom compared with our 20% threshold in the next 12-18 months.

PRIMARY CREDIT ANALYST

Florent Blot, CFA

Paris

+ 33 1 40 75 25 42

florent.blot
@spglobal.com

SECONDARY CONTACT

Marta Bevilacqua

Milan

+ (39)0272111298

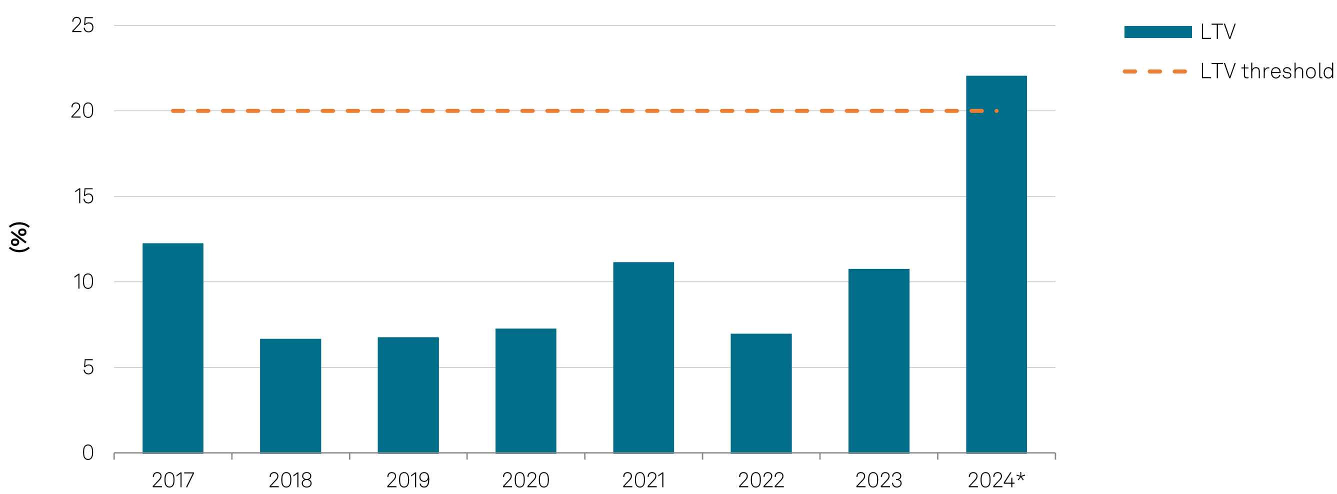
marta.bevilacqua
@spglobal.com

Rating Action Rationale

The Monroe Capital acquisition erodes Wendel's LTV headroom for the 'BBB' rating. We estimate an adjusted LTV of 21%-23% pro forma the announced acquisition, which is above the 20% maximum level for the 'BBB' rating. Although we anticipate the LTV spike to be temporary, we think that it will leave Wendel with less room to maneuver in the next 12-18 months, especially in a scenario of volatile market conditions and asset valuations. Our adjusted LTV calculation incorporates the initial cash consideration ($1.13 billion) due at closing, the deferred consideration (maximum amount of $255 million), capital commitments toward Monroe hovering around $200 million and to be deployed shortly after closing as well as the put option on the remaining 25% of capital, with an estimated value in the $350 million-$400 million range. We consider the put option payable in three instalments over 2028-2032 as a debt-like obligation mainly because it can only be settled in cash, unlike the put option held by IK Partners' 49% minority shareholders which can be paid by Wendel with its own shares at its discretion. In addition, while Wendel indicated it could invest up to $1 billion in Monroe Capital's future fundraises, we anticipate that the bulk of these soft commitments will be activated gradually over time, after an initial $200 million capital deployment in 2025.

Chart 1

The planned acquisition of Monroe Capital increases Wendel's LTV above historical levels



*As of Sept. 30, 2024 and pro-forma the acquisition of Monroe Capital. All figures adjusted by S&P Global Ratings.
LTV--Loan to value. Source: S&P Global Ratings.

We anticipate Wendel will prioritize organic deleveraging to restore LTV headroom. The investment holding's financial policy framework includes a commitment to maintain an investment-grade rating, based on which we think that management will be driving LTV below 20% in the next 12-18 months as it focuses on integrating Monroe Capital into its third-party asset management platform. Before the acquisition of Monroe, Wendel has had a track record of active asset rotation and prudent LTV management (average of about 9% since 2017 to date). We also expect Wendel's financial policy to remain relatively conservative as its targeted increase in its dividend payout (from 2.5% of its reported net asset value (NAV) in 2024 to 3.5% in the medium term) is tied to a planned growth in recurring fee related earnings (FRE) above €150 million by 2027 (on a pre-tax basis), from about €30 million with IK Partners alone and about €100 million pro forma the integration on Monroe Capital.

The growth of Wendel's asset management platform supports its recuring income and cash flow adequacy ratio. With the acquisition of Monroe Capital, we think that Wendel's third party asset management platform will gain critical mass, with total pro forma asset under management (AUM) of about €31 billion. Monroe Capital's AUM has notably grown at a 28% compound annual growth rate since 2013, from about $1.5 billion to $19.5 billion as of June 30, 2024, while IK

Partners' AUM grew to €12.2 billion as of Dec. 31, 2023 from €3.7 billion in 2014. We anticipate future fund raises at the two entities to likely support steady growth in FRE, which should ultimately support Wendel's share of recuring cash income and cash flow adequacy ratios. Pro forma the acquisition of Monroe, we estimate that Wendel's asset management platform pre-tax FRE will increase to about €100 million in 2025 from around €30 million with IK Partners alone. We anticipate that this would result in a sound cash flow adequacy ratio of around 1.5x in 2025, assuming stable dividends from Bureau Veritas (BV) and no special dividends from other principal investments.

Wendel is increasing its portfolio diversity through active asset rotation and value creation. The recent acquisitions of principal investments Scalian for €557 million and Globeducate for €625 million have notably be funded by the €1.1 billion sale of Constantia Flexibles completed in January and which represented proceeds of about 2.0x of Wendel's initial investment. In addition, the sale of a 9% stake in BV in April for €1.1 billion largely covers the initial investments for the acquisition of Monroe Capital. Overall, we view Wendel's reduced concentration on BV (about 35% of pro forma portfolio from 45% as of Dec. 31, 2023) and increasing asset diversity as favorable, including in the asset management industry. We estimate that Wendel's three largest assets represent about 62% of its pro forma portfolio value, declining from about 73% as of Dec. 31, 2023. We treat Wendel's acquisitions of IK Partners and Monroe Capital as regular portfolio investments because we anticipate that they will continue to operate as separate entities for now, with the aim to provide recurring dividend income at the investment holding level.

Outlook

The negative outlook on Wendel reflects the risk of a downgrade if its adjusted LTV stays above 20% in the next 12-18 months because of weaker market conditions or it fails to restore greater financial flexibility from organic deleveraging.

Downside scenario

We could lower our rating on Wendel if its adjusted LTV ratio stayed above 20% with no prospect of a rapid recovery. Although less likely with the acquisitions of IK Partners and Monroe Capital, we could also lower the rating over the medium term if Wendel's cash flow adequacy dropped below 0.7x and its cash position diminished such that cash reserves did not abundantly compensate its operating deficit.

Upside scenario

We could revise our outlook on Wendel to stable if the company restored adequate LTV headroom compared with our 20% downside threshold, with management committing to maintain such levels sustainably.

Company Description

Wendel is a France-based investment holding company, tracing its history back to the eighteenth-century steel industry in eastern France. As of Sept. 30, 2024, we estimate that its adjusted investment portfolio was about €10.4 billion pro forma the planned acquisitions of

Globeducate and Monroe Capital, and investment commitments. The holding is invested in diversified sectors such as business services, chemicals, asset management, flooring materials, and telecommunications across Europe, North America, and Africa. Key investments include a 26.5% stake in publicly listed testing, inspection, and certification business BV (about 35% of pro forma portfolio value), and a 68.1% stake in leather chemicals and specialty coatings producer Stahl.

Wendel is publicly listed on the Paris stock exchange. With 39.6% as of Sept. 30, 2024, Wendel-Participations SE, a family vehicle representing the individual interests of more than 1,200 Wendel family members, holds the largest stake in the company and has 52.6% of voting rights. Six members of the Wendel family are on the supervisory board.

Our Base-Case Scenario

Assumptions

- LTV of 21%-23% pro forma the acquisition of Monroe Capital and gradually decreasing below 20% as Wendel prioritizes organic deleveraging.
- Dividend income of about €200 million in 2024-2025, supported by dividends from BV and the special dividend from the Crisis Prevention Institute in 2024 and growth in FRE in 2025.
- Annual operating costs below €100 million.
- Net interest expense of €15 million-€20 million in 2025 after a temporary surplus in 2024.
- Cash dividends to Wendel's shareholders of about €173 million in 2024 (€4.0 per share based on 2023 results), in line with the company's payout target of 2.5% of its NAV. Dividends paid were €3.2 per share in 2023, up from €3.0 in 2022. We anticipate future dividend growth to be tied to Wendel's asset management platform FRE growth.
- We anticipate limited share repurchases under the company's new €100 million share buyback program in the next months. Wendel completed its previous €100 million program launched in October 2023 in July 2024.

Key metrics

Table 1

Wendel SE--Key metrics

Period ending	2017a	2018a	2019a	2020a	2021a	2022a	2023a	2024f*
LTV (%)	12.2	6.6	6.7	7.2	11.1	6.9	10.7	21.0-23.0
Cash flow adequacy (x)	1	0.6	0.0	0.0	0.5	0.7	1.8	1.6-1.8

All figures are adjusted by S&P Global Ratings, unless stated as reported. *Pro-forma the acquisition of Monroe Capital and Globeducate as well investment commitments. a--Actual. f--Forecast

Liquidity

Our assessment of Wendel's liquidity as strong reflects our expectation that its liquidity sources will likely exceed liquidity uses by about 1.6x in the next 12 months, and about 1.4x over the subsequent 12 months. Wendel's generally good access to the bond market, solid relations with banking counterparties, and comfortable headroom under covenants further support our assessment.

Principal liquidity sources for the next 24 months starting Oct. 1, 2024:

- Net cash and cash equivalents of about €3.0 billion;
- Full availability under the €875 million revolving credit facility (RCF) expiring in 2029; and
- Dividend income of about €200 million per year.

Principal liquidity uses for the same period:

- No debt maturities in first 12 months and about €960 million in the subsequent 12 months;
- Operating expenses of about €90 million-€100 million per year;
- Interest expenses of €15 million-€20 million per year;
- Annual dividend payment to Wendel's shareholders of at least €175 million; and
- About €2.2 billion of cashout for the acquisitions of Globeducate and Monroe Capital, as well as for investment commitments toward IK Partners and Monroe Capital.

Covenants

Wendel's €875 million RCF bears two LTV covenants, tested semiannually only if the line is drawn down. As the line is undrawn, there is no obligation of covenant headroom reporting, but we estimate that the headroom would be comfortable in the case of RCF drawdowns.

Environmental, Social, And Governance

Environmental, social, and governance factors are an overall neutral consideration in our credit rating analysis of Wendel. The holding benefits from a diversified portfolio of assets, with a concentration on business services through its stake in BV, which accounts for close to 35% of the portfolio value, and limited exposure of investee companies to environmental or social risks. We regard Wendel's governance as robust enough to sustain the holding's investment and divestment policies and as such consider it neutral to our ratings on Wendel.

Issue Ratings - Subordination Risk Analysis

Capital structure

On Sept. 30, 2024, Wendel's capital structure consisted of about €2.4 billion of senior unsecured debt issued at the holding company level, including the €750 million issue of bonds exchangeable into BV shares. Wendel's undrawn RCF is also unsecured.

Analytical conclusions

The issue rating on Wendel's senior unsecured notes is 'BBB', the same as the long-term issuer credit rating, because there are no significant elements of subordination risk present in Wendel's capital structure.

Ratings Score Snapshot

Issuer Credit Rating	**BBB/Negative/A-2**
Business risk:	Fair
Country risk	Low
Industry risk	Intermediate
Competitive position	Fair
Financial risk:	Modest
Cash flow/leverage	Modest
Anchor	bbb-
Modifiers:	
Liquidity	Strong (no impact)
Management and governance	Neutral (no impact)
Comparable rating analysis	Positive (+1 notch)
Stand-alone credit profile:	bbb

Related Criteria

- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | Industrials: Methodology: Investment Holding Companies, Dec. 1, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013

- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Economic Research: Global Economic Outlook Q4 2024: So Far, So Smooth--Can It Last?, Sept. 26, 2024
- Bulletin: Wendel's Sale Of A Partial Stake In Bureau Veritas Unlocks Greater Financial Flexibility, April 12, 2024
- Research Update: Safeguard Purchaser LLC (dba Crisis Prevention Institute) Assigned 'B-' Rating; Outlook Stable; Debt Rated 'B-', March 19, 2024

Ratings List

Outlook Action; Ratings Affirmed

	To	From
Wendel SE		
Issuer Credit Rating	BBB/Negative/A-2	BBB/Stable/A-2
Senior Unsecured	BBB	